

STATE-GUARANTEED REAL ESTATE LOANS MADE BY
NATIONAL BANKS

JULY 13, 1959.—Ordered to be printed

Mr. MUSKIE, from the Committee on Banking and Currency, submitted the following

REPORT

[To accompany S. 1173]

The Committee on Banking and Currency, to whom was referred the bill (S. 1173) to amend section 24 of the Federal Reserve Act to exempt real estate loans guaranteed by States from its provisions, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

PURPOSE OF THE BILL

The purpose of the bill is to authorize national banks to make real estate loans guaranteed by the faith and credit of a State, without regard to the restrictions imposed by section 24 of the Federal Reserve Act on the terms of individual real estate loans. This will enable national banks to make loans for industrial development projects where the applicable State law provides that the State or a State agency can pledge the State's faith and credit to meet the obligation.

GENERAL STATEMENT

Section 24 of the Federal Reserve Act authorizes national banks to make real estate loans secured by first liens on improved real estate. Two types of limitations are imposed on such real estate loans. First, the amount of the loan on an individual piece of real estate may not exceed specified percentages of the appraised value of the real estate and the duration of the loan may not exceed specified periods (50 percent of the appraised value, up to 5 years; or 66⅔ percent, up to 10 years, if 40 percent amortized; or 66⅔ percent, up to 20 years, if fully amortized). These limitations are based on the need to provide assurance against loss to the bank on the individual loan. Second, a limitation is imposed on the aggregate amount of real estate loans

which a bank may make (not more than the amount of its capital stock paid in and unimpaired plus the amount of its unimpaired surplus fund, or 60 percent of its time and savings deposits, whichever is greater). These limitations are imposed in order to assure the bank's liquidity.

The limitations applicable to individual loans, designed to protect the bank against loss on the individual loan, are waived in the case of real estate loans which are insured under title II, title VI, title VIII, section 8 of title I, or title IX of the National Housing Act, or which are insured under title I of the Bankhead-Jones Farm Tenant Act, or which are insured under the act of August 28, 1937, which relates to water storage and utilization facilities, or for veterans' loans guaranteed under the Servicemen's Readjustment Act of 1944. Clearly, a bank may make a real estate loan without risk of loss, regardless of the percentage of the appraised value of the real estate involved or the duration of the loan, if the Federal Government insures the loan. An exemption is not provided, however, with respect to these federally insured loans, from the limitations of section 24 on the aggregate amount of real estate loans, because the assurance against loss provided by Federal guarantee of a loan does not assure the bank's liquidity.

The committee has been advised that the Maine Industrial Building Authority and the Rhode Island Industrial Building Authority have authority to guarantee loans on industrial properties up to 90 percent of their cost, and that the faith and credit of the respective States are pledged to meet the obligations of their building authorities. Section 24, however, prevents national banks from participating in these loans, except within the restrictions imposed by that section.

These State industrial building authorities are considered by their sponsors as important instruments for the development and progress of the economies of those States. The banks of these States are ready and willing to participate in the projects sponsored by these authorities. State banks can do so, because section 24 of the Federal Reserve Act applies only to national banks. There is no reason for a restriction which prevents national banks from taking their part in these programs too.

S. 1173 would amend section 24 of the Federal Reserve Act so as to exempt, from the limitations applicable to individual loans, those real estate loans which are 100 percent guaranteed or insured by a State or by a State authority for the payment of whose obligations the faith and credit of the State is pledged. These State-guaranteed loans would thereby be placed in the same position as loans guaranteed under the National Housing Act and other Federal programs. However, the limitations imposed by section 24 of the Federal Reserve Act on the aggregate amount of real estate loans which a bank might make, which are important from the point of view of the bank's liquidity, would not be waived by S. 1173.

The amendment which would be made by S. 1173 is not, of course, limited to the two industrial building authorities mentioned above. It may be expected that other authorities of this sort will be created by other States, if these prove effective. And the amendment is not limited to loans guaranteed by authorities of this sort. The amendment covers all real estate loans which are 100 percent guaranteed by a State or by a State agency for whose obligations the State's faith

and credit is pledged. Since the only purpose of the restriction which is being waived is to prevent the bank from loss on the individual loan, and since a guarantee by a State is ample assurance against loss on the loan, there is no need to limit the scope of the exception, so long as the faith and credit of a State is behind the loan.

The Federal Reserve Board and the Federal Deposit Insurance Corporation have recommended enactment of S. 1173, and the Treasury Department has advised that it has no objection to its enactment. The Governor of the State of Maine and the chairman of the Rhode Island Industrial Building Authority have recommended enactment of S. 1173. Letters from the agencies and from the Governor of the State of Maine and the Rhode Island Industrial Building Authority in support of S. 1173 are printed at the end of this report.

COMMITTEE AMENDMENTS

The committee has made three amendments to the bill, which were recommended by the Federal Reserve Board and approved by the Treasury Department and the Federal Deposit Insurance Corporation.

The first amendment, deleting the words "and shall not apply to real estate loans" and substituting the word "or" is merely an editorial change to obviate duplication of words already in the statute.

The second amendment substitutes the word "loan" for the word "mortgage" in the proviso requiring that under the terms of the guarantee, the bank will be assured of repayment in accordance with the terms of the loan. Ordinarily, the mortgage itself does not contain the terms of the loan, which usually are contained in the note or bond which is secured by the mortgage or trust deed.

The title of the bill is amended to specify that the only restrictions which are waived for State guaranteed loans are the restrictions applicable to individual loans. The restrictions contained in section 24 on the aggregate amount of real estate loans which a bank may make are not waived.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Washington, March 25, 1959.

HON. A. WILLIS ROBERTSON,
Chairman, Committee on Banking and Currency,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your two letters of February 27, 1959, requesting reports by the Board of Governors on S. 1173, a bill to amend section 24 of the Federal Reserve Act to exempt real estate loans guaranteed by States from its provisions, and S. 1174, a bill to amend section 24 of the Federal Reserve Act to provide that the existing restrictions on the amount and maturity of real estate loans made by national banks shall not apply to certain loans which are guaranteed or insured by a State or a State authority. Since these two bills are similar in their purposes and effect, the comments offered by the Board in this report will apply to both bills unless otherwise indicated.

S. 1173 is identical with the bill S. 3561, introduced in the 85th Congress, with respect to which the Board reported to the Senate Banking and Currency Committee by letter dated April 17, 1958. In that report the Board expressed its views substantially as follows.

The third sentence of section 24 of the Federal Reserve Act places maximum limits upon (1) the maturity of loans by national banks upon the security of real estate and (2) the amount that may be lent in relation to the appraised value of real estate securities. S. 1173 would exempt from these limits real estate loans which are 100 per centum guaranteed or insured by a State or by a State authority for the payment of the obligations of which the faith and credit of the State is pledged.

The provisions of the third sentence of section 24 are designed to prevent national banks from making real estate loans that might involve an undue risk of loss. Where a loan is supported by the credit of a State there would not appear to be any significant risk even if the loan is for a period exceeding the maximum prescribed in section 24 or for a larger percentage of the value of the real estate security than would be permissible under that section. Accordingly, the Board of Governors favors the objective embodied in S. 1173.

The fourth sentence of section 24 prescribes limitations upon the aggregate amount of real estate loans that may be made by a national bank. One purpose of these provisions is to help safeguard national banks' liquidity. The backing of a State would not necessarily assure the liquidity of a long-term real estate loan but that question does not arise under either S. 1173 or S. 1174, since the aggregate limitations would not be affected thereby. However, the title of S. 1173 would suggest that the loans of the kind described are to be exempt from all provisions of section 24. Accordingly, if your committee is inclined to approve S. 1174 rather than S. 1173, you may consider it advisable to substitute the title of S. 1174 for the present title of S. 1173 since the title of S. 1174 clearly limits the application of the bill to the existing restrictions on the amount and maturity of real estate loans made by national banks.

It has been noted that S. 1174 differs from S. 1173 in two respects. S. 1173 makes it clear that the amendment to section 24 applies to real estate loans which are 100 percent guaranteed and also contains the proviso that under the terms of the guarantee or insurance agreement, the national bank will be assured of repayment in accordance with the terms of the mortgage. The Board considers that in these two respects the language of S. 1173 is preferable to that of S. 1174.

It might also be desirable for the sake of clarity and uniformity (1) to substitute the word "or" for the words "and shall not apply to real estate loans" in the body of the bills and (2) to substitute the word "loan" for the word "mortgage" at the end of the proviso in S. 1173.

Sincerely yours,

C. CANBY BALDERSTON, *Vice Chairman.*

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, April 24, 1959.

HON. A. WILLIS ROBERTSON,
Chairman, Committee on Banking and Currency,
U.S. Senate, Washington, D.C.

DEAR SENATOR ROBERTSON: We have your request for our views on S. 1173, a bill which would exempt real estate loans which are 100 percent guaranteed or insured by a State or by a State authority

from the limitations and restrictions on real estate loans by national banks other than the limitation on total real estate loans.

It is our view that the proposed bill is in accord with sound banking practices, and that its enactment would be in the public interest. Accordingly, the Corporation recommends the enactment of this bill.

We have been advised by the Bureau of the Budget that it has no objection to the submission of this report.

Sincerely yours,

JESSE P. WOLCOTT, *Chairman.*

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, July 10, 1959.

Re S. 1173

Hon. A. WILLIS ROBERTSON,
Chairman, Committee on Banking and Currency,
U.S. Senate, Washington, D.C.

DEAR SENATOR ROBERTSON: Under date of April 24, we advised you that the enactment of S. 1173, or a companion bill, S. 1174, both met with the approval of the Corporation. However, we stated we preferred the language of S. 1173.

We are advised that you have received a communication from the Board of Governors of the Federal Reserve System approving the S. 1173, but suggesting the title be changed to correspond with the title of S. 1174. Likewise, the Board has suggested two language changes in the bill: (1) the substitution of the word "or" for the words "and shall not apply to real estate loans" and (2) the substitution of the word "loan" for the word "mortgage" at the end of the proviso.

For the purposes of clarity and uniformity, we would endorse the changes above mentioned. Further, we recommend the enactment of S. 1173 containing the proposed amendments.

Sincerely yours,

JESSE P. WOLCOTT, *Chairman.*

TREASURY DEPARTMENT,
April 22, 1959.

Hon. A. WILLIS ROBERTSON,
Chairman, Committee on Banking and Currency,
U.S. Senate, Washington, D.C.

MY DEAR MR. CHAIRMAN: Reference is made to your letters of February 27, 1959, in which you request the views of this Department on S. 1173, a bill to amend section 24 of the Federal Reserve Act to exempt real estate loans guaranteed by States from its provisions, and S. 1174, a bill to amend section 24 of the Federal Reserve Act to provide that the existing restrictions on the amount and maturity of real estate loans made by national banks shall not apply to certain loans which are guaranteed or insured by a State or a State authority.

S. 1173 would amend section 24 of the Federal Reserve Act so as to exempt from the restrictions and limitations contained in that

section with respect to appraisal and maturity requirements, loans 100 percent guaranteed or insured by a State or State authority for the payment of the obligations of which the faith and credit of the State is pledged: provided, that under the terms of the guarantee or insurance agreement the association will be assured of repayment in accordance with the terms of the loan. S. 1174 would amend section 24 of the Federal Reserve Act so as to exempt from the restrictions and limitations contained in that section with respect to appraisal and maturity requirements, loans guaranteed or insured by a State or a State authority for the payment of the obligations of which the faith and credit of the State is pledged.

The two bills appear to be designed to accomplish the same result, although S. 1174 does not specifically require that the loans be 100 percent guaranteed, and omits the proviso contained in S. 1173. Thus, it appears that if S. 1173 is enacted, there will be no need to enact S. 1174. The purpose of S. 1173 is to permit national banks in the State of Maine to participate in real estate loans insured by the Maine Industrial Building Authority. Such loans will be made to construct industrial projects, and under the Maine statute such loans may be made up to 90 percent of the cost of the projects, in amounts up to \$1 million, and with maturities of up to 25 years. Such loans may be insured by the Maine Industrial Building Authority. The faith and credit of the State of Maine is pledged to meet the obligations of the building authority. The Maine statute specifically authorizes the Governor and the council to transfer to the authority from the State contingent account or from the proceeds of bonds which may be insured by the State up to \$20 million, amounts necessary to meet the obligations of the mortgage insurance fund.

Since, in order to qualify for exemption from section 24 under the proposed legislation, the guarantee or insurance required will have to be, in effect, the equivalent of general obligations of the State involved, this Department has no objection to the enactment of S. 1173. We would not favor enactment of S. 1174.

The Department has been advised by the Bureau of the Budget that there is no objection to the submission of this report to your committee.

Very truly yours,

LAURENCE B. ROBBINS,
Acting Secretary of the Treasury.

TREASURY DEPARTMENT,
July 8, 1959.

Hon. A. WILLIS ROBERTSON,
Chairman, Banking and Currency Committee, U.S. Senate, Washington, D.C.

MY DEAR SENATOR ROBERTSON: Reference is made to S. 1173, a bill to amend section 24 of the Federal Reserve Act, which is now pending before your committee. It has come to our attention that the Board of Governors of the Federal Reserve System has recommended three changes in this proposed legislation, one being a change in its title, and the other two being minor changes of a clarifying nature.

The purpose of this letter is to advise you that this Department is in agreement with the recommendations of the Board, and we would have no objection to their adoption by your committee.

Very truly yours,

LAURENCE B. ROBBINS,
Acting Secretary of the Treasury.

STATE OF MAINE,
OFFICE OF THE GOVERNOR,
Augusta, July 10, 1959.

Hon. A. WILLIS ROBERTSON,
*Chairman, Senate Committee on Banking and Currency,
Senate Office Building, Washington, D.C.*

DEAR SENATOR ROBERTSON: I would like this letter to be considered in strong support of S. 1173, introduced by Senator Edmund S. Muskie, and which I understand has been reported out favorably by your committee.

Early in 1958 the State of Maine established a Maine Industrial Building Authority following action taken late in 1957 at a special session of our legislature. Through this vehicle the full faith and credit of the State of Maine is pledged on certain first mortgages for industrial buildings, and our experience has proven that national banks in Maine have been operating at a disadvantage inasmuch as the Federal Reserve Act (12 U.S.C. 371, sec. 24) eliminates their participation in this type of loan.

Since the activation of the Maine Industrial Building Authority, the State of Rhode Island has activated a similar authority and legislation is currently in progress in the State of Michigan for a third such authority. National banks in these other two areas are going to be at the same disadvantage as they are currently in Maine, and these States are going to feel the lack of investment capital due to the ineligibility of the national banks to participate in their program.

For these reasons, I strongly recommend to the committee passage of your amendment to section 24 of the Federal Reserve Act.

With kindest regards, I am,

Sincerely,

CLINTON A. CLAUSON, *Governor.*

THE TOP CO., INC.,
Woonsocket, R.I., May 21, 1959.

Hon. THEODORE FRANCIS GREEN,
Senate Office Building, Washington, D.C.

DEAR SENATOR GREEN: I am writing you at this time as chairman, and in behalf of the Rhode Island Industrial Building Authority which, as you know, insures mortgage payments on new industrial properties up to 90 percent of their cost (not to exceed \$1,750,000 in any one project). This, with funds from other sources, provides for 100 percent financing of new plants.

I have been led to understand that under section 24 of the Federal Reserve Act, national banks are prevented from making a loan which exceeds two-thirds of the appraised value. This means that the

Industrial National Bank of Providence, our largest Rhode Island lending institution, cannot participate solely in the 90-percent loans to which we have pledged the State's credit.

On February 26, 1959, a bill S. 1173, was introduced in the Senate which would amend section 24 of the Federal Reserve Act to allow national banks to go up to 90 percent of the cost of a project provided the loan was guaranteed by the State. We of the authority hope you will give this bill your active support as it is of very real importance to the State as well as to the lending institutions. The Treasury and the American Bankers Association have both given their endorsed support of this bill.

With kindest personal regards, I remain,

Sincerely yours,

ARTHUR L. DARMAN.

CHANGES IN EXISTING LAW

In compliance with subsection (4) of rule XXIX of the Standing Rules of the Senate, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

FEDERAL RESERVE ACT

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SEC. 24. Any national banking association may make real estate loans secured by first liens upon improved real estate, including improved farmland and improved business and residential properties. A loan secured by real estate within the meaning of this section shall be in the form of an obligation or obligations secured by a mortgage, trust deed, or other instrument upon real estate, which shall constitute a first lien on real estate in fee simple or, under such rules and regulations as may be prescribed by the Comptroller of the Currency, on a leasehold (1) under a lease for not less than ninety-nine years which is renewable or (2) under a lease having a period of not less than fifty years to run from the date the loan is made or acquired by the national banking association, and any national banking association may purchase any obligation so secured when the entire amount of such obligation is sold to the association. The amount of any such loan hereafter made shall not exceed 50 per centum of the appraised value of the real estate offered as security and no such loan shall be made for a longer term than five years; except that (1) any such loan may be made in an amount not to exceed 66% per centum of the appraised value of the real estate offered as security and for a term not longer than ten years if the loan is secured by an amortized mortgage, deed of trust, or other such instrument under the terms of which the installment payments are sufficient to amortize 40 per centum or more of the principal of the loan within a period of not more than ten years, (2) any such loan may be made in an amount not to exceed 66% per centum of the appraised value of the real estate offered as security and for a term not longer than twenty years if the loan is secured by an amortized mortgage, deed of trust, or other

such instrument under the terms of which the installment payments are sufficient to amortize the entire principal of the loan within a period of not more than twenty years, and (3) the foregoing limitations and restrictions shall not prevent the renewal or extension of loans heretofore made and shall not apply to real estate loans which are insured under the provisions of title II, title VI, title VIII, section 8 of title I, or title IX of the National Housing Act or which are insured by the Secretary of Agriculture pursuant to title I of the Bankhead-Jones Farm Tenant Act, or the Act entitled "An Act to promote conservation in the arid and semiarid areas of the United States by aiding in the development of facilities for water storage and utilization, and for other purposes", approved August 28, 1937, as amended, *or which are 100 per centum guaranteed or insured by a State or by a State authority for the payment of the obligations of which the faith and credit of the State is pledged: Provided, That under the terms of the guaranty or insurance agreement the association will be assured of repayment in accordance with the terms of the loan.* No such association shall make such loans in an aggregate sum in excess of the amount of the capital stock of such association paid in and unimpaired plus the amount of its unimpaired surplus fund, or in excess of 60 per centum of the amount of its time and savings deposits, whichever is the greater. Any such association may continue hereafter as heretofore to receive time and savings deposits and to pay interest on the same, but the rate of interest which such association may pay upon such time deposits or upon savings or other deposits shall not exceed the maximum rate authorized by law to be paid upon such deposits by State banks or trust companies organized under the laws of the State in which such association is located.

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